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July 12, 2002

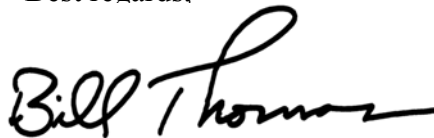
The Honorable Richard K. Armey
Chairman
Select Committee on Homeland Security
H-226, the Capitol
Washington, DC 20515

Dear Mr. Chairman:

As specified in Section 6 of H. Res. 449, this letter transmits the views and recommendations of the Committee on Ways and Means on those aspects within the jurisdiction of the Committee of the bill, H.R. 5005, to establish a Department of Homeland Security and transfer the United States Customs Service to the new Department. The recommended legislative text is attached and was favorably reported from the Committee on July 10, 2002.

The Committee on Ways and Means looks forward to working with the Select Committee on Homeland Security as we promote security while maintaining the free flow of trade across American borders.

Best regards,



Bill Thomas
Chairman

WMT/dkk

I. INTRODUCTION

A. Background on the United States Customs Service

Since 1789, the United States Customs Service has been a federal agency under the United States Treasury Department. Congress created the Customs Service as its fifth legislative act in order to implement the first Act of Congress, the Tariff Act of 1789. Virtually all federal government revenue was originally collected by the Customs Service through duties. Today, the Customs Service collects over \$20 billion of revenue, ensures that all imports and exports comply with U.S. laws and regulations, guards against smuggling, and is responsible for the following:

1. Assessing and collecting customs duties, excise taxes, fees and penalties due on imported merchandise;
2. Interdicting and seizing contraband, including narcotics and illegal drugs;
3. Processing persons, baggage, cargo and mail, and administering certain navigation laws;
4. Detecting and apprehending persons engaged in fraudulent practices designed to circumvent customs and related laws;
5. Protecting American business and labor and intellectual property rights by enforcing U.S. laws intended to prevent illegal trade practices, including provisions related to quotas and the marking of imported merchandise;
6. Collecting anti-dumping and other duties under our trade remedies laws and by providing customs recordation for copyrights, patents and trademarks;
7. Protecting the general welfare and security of the United States by enforcing import and export restrictions and prohibitions, including the export of critical technology used to develop weapons of mass destruction, and money laundering; and
8. Collecting accurate import and export data for compilation of international trade statistics.

Today, in addition to its own laws, the Customs Service enforces well over 400 other provisions of law for at least 40 agencies. A number of these statutes relate to quality of life issues involving the environment, such as motor vehicle safety and emission controls, water pollution standards, pesticide controls, freon smuggling, and the protection of endangered wildlife. Other laws safeguard American agriculture, business and public health, and consumer safety.

B. The President's Homeland Security Proposal and H.R. 5005

On June 18, 2002, President Bush proposed to transfer all of the authority and assets of the Customs Service, as well as many other federal agencies, to a new Department of Homeland Security. This proposal was incorporated into H.R. 5005, which was introduced on June 24, 2002. Specifically, the Customs Service would be placed under an Under Secretariat for Border and Transportation Security along with the Immigration and Naturalization Service, the Animal and Plant Health Inspection Service, the Coast Guard, and the Transportation Security Administration. Unlike the Coast Guard, H.R. 5005 does not require that the Customs Service be maintained as a separate entity. Under Section 402 of H.R. 5005, the Secretary of Homeland Security would be vested in the functions, personnel, assets, and liabilities of the United States

Customs Service of the Department of the Treasury, including the functions of the Secretary of the Treasury relating thereto. The President's proposal would give the Secretary significant authority to reorganize the Customs Service, reallocate reserves within Customs, and make changes to Customs employees' compensation.

C. Rationale for the Committee's Recommendations to Amend H.R. 5005

Unlike other agencies that are being transferred to the new Department of Homeland Security, the Customs Service has four unique characteristics:

1. The Customs Service is a revenue-collecting agency with significant trade facilitation functions. The Customs Service collects over \$20 billion a year in duties, second only to the Internal Revenue Service in collections. Economically critical trade laws are implemented by the Customs Service. Because of its border presence, the Customs Service has taken on other border-related missions such as preventing drug smuggling and stopping weapons of mass destruction.
2. A significant portion of the Customs Service's budget is funded through over \$1 ½ billion worth of user fees paid by importers, and by law those fees must be used only for specific inspectional services or as budgetary offsets to general commercial operations.
3. Most of the Customs Service's legal authority is held by the Treasury Department or other agencies of government and delegated to the Customs Service. For example, 19 U.S.C. 3 states that the Secretary of the Treasury shall supervise the collection of duties. Historically, this responsibility has been delegated to the Customs Service.
4. Substantial portions of the Customs Service's trade work is very technical and esoteric. The work requires professionals with legal and regulatory skills that are unlike border security skills.

For these reasons, the Members of the Committee recommend that the Select Committee on Homeland Security recognize the unique mission of the Customs Service and adopt the attached bill language to amend H.R. 5005. In making these recommendations, the Committee adopts the fundamental basis for of the President's proposal and agrees to transfer Customs assets and personnel in their entirety to the new Department of Homeland Security. The Committee rejected the option of carving up the Customs Service into commercial and non-commercial elements. Instead, the Committee sought to identify and prevent further reorganization or reductions in a closely defined core group that perform revenue-collection functions.

The Committee was guided by one over-riding goal: to ensure that the Department of Homeland Security would be successful and not hamstrung by any limits on its authority or ability to carry out the protection of Americans. It is also important to ensure that revenue continues to be collected and that goods keep moving across the border with little delay in order to maintain delicately balanced commercial schedules and operations. The Committee is confident that the proposed changes to H.R. 5005 do not interfere with the new Department's missions but will enhance its effectiveness.

Four amendments were offered to the Chairman's mark. The first amendment, offered by Mr. Cardin, would have designated the existing Customs Service as a "distinct entity" within the Homeland Security Department. This amendment failed by voice vote. The second amendment, offered by Mr. Becerra, would have expanded the dedicated use provision for the merchandise processing fee (MPF) in the Chairman's mark to require use of MPF receipts (in excess) of the \$350 million dedicated for ACE development) for commercial operations. This amendment failed by a roll call vote of 12 ayes to 24 noes. The third amendment, offered by Mr. McDermott, would have preserved existing and future Customs' employees pay, performance standards, etc. as provided under Title 19 and Title 5. This amendment failed by a voice vote. Mr. Doggett offered an amendment to prohibit the Customs Service from entering into contracts with companies that have reincorporated overseas in order to avoid U.S. taxation. This amendment was agreed to without objection.

II. EXPLANATION OF RECOMMENDATIONS TO AMEND H.R. 5005

Sec. 402 of base text: The recommendation would authorize the transfer of functions, personnel, assets, and liabilities of the existing Customs Service in their entirety to the Division for Border and Transportation Security of the Department of Homeland Security, subject to other provisions of the amendment. Unlike H.R. 5005, the Committee does not recommend transferring the functions of the Department of the Treasury related to the Customs Service for the reasons given below in Sections 411 and 412.

Sec. 411: A core Customs Service is established within the Department of Homeland Security and vested, at a minimum, with certain revenue-related offices and functions as specifically identified. This core Customs entity will continue to have a Senate-confirmed Commissioner, and the incumbent Commissioner may continue to serve until a new Commissioner is named.

The primary function of the Customs Service has always been revenue collection and trade facilitation, and it is imperative to maintain these activities. However, revenue and trade will be relatively minor activities within the very large, new Department of Homeland Security. Given the importance of trade and government revenue, an independent and separate Congressional mandate for trade and revenue collection is appropriate. Accordingly, Customs Service personnel and offices that handle these unique revenue and trade functions should continue to operate within their organization after the transfer to the new Department.

This section refers to Section 420(7) of the amendment for the list of components within the current Customs Service that the Committee determines to be completely or primarily devoted to the performance of revenue collection: Import Specialists, Entry Specialists, Drawback Specialists, National Import Specialists, Fines and Penalties Specialists, attorneys of the Office of Regulations and Rulings, Customs Auditors, International Trade Specialists, and Financial Systems Specialists. The personnel who perform this work have specialized skills in the very technical field of trade law, which are unlike the skills related to border security. For this reason, the group identified in Section 420(7) would comprise the Customs Service core established under Section 411 within the Department of Homeland Security and would have a distinct existence apart, though integrated with, the many border security elements of the new Department.

Regarding the provision requiring a Senate confirmed Customs Commissioner, the Committee

believes that the person who leads the Customs Service must be an extraordinary individual to handle the multiple functions of that office. The Commissioner should continue to answer to, and be endorsed by Congress to ensure that all of Customs' missions are recognized.

Sec. 412(a): The recommendation would reserve revenue collecting statutory authority to Treasury, where it is currently vested, and transfer all other authority exercised by the existing Customs Service to the Department of Homeland Security. Treasury may delegate its reserved authority to Homeland Security, as it often does to Customs today. Treasury shall consult with Homeland Security on all matters and regulations affecting customs functions. The recommendation authorizes the Department of the Treasury to hire additional staff to exercise this authority.

It is not unusual for the Customs Service to implement and enforce laws that by statute are intended to be implemented by entirely different departments; indeed, Customs Service currently enforces 400 laws on behalf of 40 different agencies. The proposed changes would continue to empower the Secretary of the Treasury to promulgate regulations on a myriad of highly technical trade matters, while leaving it to the new Department of Homeland Security to implement them. In this way, Treasury's trade expertise and macroeconomic outlook is retained to address technical trade matters.

Sec. 412(b): With regard to the Customs Service core established under Section 411, reorganization or decrease in the funding or staff or reductions to Title 5 pay and benefits levels is prohibited in order to preserve these critical trade functions.

The President and Governor Ridge have described their wish for flexibility in the Department structure created by Congress, and there are many ways that the Administration will be able to obtain the "synergy" it seeks for the new Homeland Security Department with the Committee's recommendations. As described earlier, however, the revenue-oriented group established under Section 411 has unique functions distinct from security functions. It is therefore appropriate to prohibit reductions to this core group and to preserve these critical trade functions.

Sec. 413: The recommendation provides that the Secretary shall maintain adequate staffing to assure that existing levels of customs revenue services are maintained, and the Secretary shall notify Congress of actions that reduce such services.

Although all offices of the Customs Service conduct revenue-collecting services, those components of Customs that are outside of the core revenue-collecting group described in Section 420(7) and required to be kept intact per Section 412(b) perform mixed functions. The Committee is mindful of the flexibility needs and security goals of the President and therefore requires only that customs revenue services, not necessarily staffing, be maintained at the existing levels as the Customs Service is transferred to the new Department of Homeland Security. Any significant reduction in services must be reported to Congress in advance, which is consistent with current law at 19 U.S.C. 2075(g).

Sec. 414: The Customs Service is required to implement a cost accounting system in order to determine and track the use of \$1.5 billion of Customs user fees.

The Committee is concerned that Customs Service is currently unable to answer fundamental

questions about how it spends money. For example, Customs officials state that it spends a certain amount of money on commercial operations. The figure is not based upon the addition of various commercial costs from all operations within the Customs Service, such as the number of people who actually processed entries of merchandise at specific ports during a set period. Instead, the figure is based upon Customs officials' belief that a set percentage of its work is always related to commercial activities. That static percentage is based upon a no longer available, ad hoc survey conducted by Customs several years ago. A modern cost accounting system would allow the Customs Service to accurately identify the amount of money spent at specific locations and for specific revenue functions.

Given that \$1.5 billion of Customs' \$2.6 billion budget comes from the collection of fees that are ostensibly for specified revenue services, the Committee adopted this provision to ensure that revenue collecting functions can be closely tracked within the overall Department of Homeland Security, with strict account for such fees. Therefore, this reform is appropriate for a bill to transfer the Customs Service to the new Department of Homeland Security.

Such a system would also provide compliance with the core financial system requirements of the Joint Financial Management Improvement Program (JFMIP), which is a joint and cooperative undertaking of the U.S. Department of the Treasury, the General Accounting Office, the Office of Management and Budget, and the Office of Personnel Management working in cooperation with each other and other agencies to improve financial management practices in government. That Program has statutory authorization in the Budget and Accounting Procedures Act of 1950 (31 U.S.C. 65).

Sec. 415: The recommendation provides that Customs fees (with the exception of the merchandise processing fee) must continue to be used for currently authorized functions. Fee receipts may not be transferred to any other agency or office in the Department.

Congress created import fees to help fund critical customs activities. Fees are paid by commercial interests in return for specific commercial services. There have long been concerns about whether Customs can adequately account for the cost of providing commercial services in return for the fees collected. See the discussion in Section 414 above. It would be inappropriate and potentially inconsistent with United States trade obligation for importers to pay fees that subsidize non-commercial functions of the new Department of Homeland Security. For these reasons, the Committee believes that fees should continue to be spent only on activities already defined in 19 U.S.C. 58c.

Sec. 416: The recommendation would make further changes for the purpose of ensuring that certain commercial functions are carried out. The text would require that all reports now provided to Congress from the Customs Service shall continue to be provided to the House Ways and Means and Senate Finance Committees.

Transferring the assets and functions of the Customs Service to the new Department of Homeland Security will not lessen the need of these committees for information about trade operations. Through the Customs Service, the Department will be implementing virtually all trade obligations of the United States. These trade obligations lie within the jurisdiction of these committees. Therefore, existing reports should continue to be provided to the Congressional committees of jurisdiction on trade to allow the committees to continue appropriate oversight

and authorizations.

Sec. 417: The recommendation provides that a portion of the Customs Merchandise Processing Fee must go to build the new Customs computer.

The Customs Service's current import system, the Automated Commercial System (ACS), was designed in 1984 and will not be able to meet the increasingly complex, long-term requirements impacted by the growth in trade, responsibilities, and legislation. Consequently, replacing ACS with the Automated Commercial Environment (ACE) is a critical component in the modernization and development of the Customs Service. The new computer system has also taken center stage in the fight against terrorism since security data collection will be an important objective of the new Department. It is therefore entirely appropriate to mandate that the ACE system be built from the proceeds of the merchandise processing fee.

This provision has strong support from the import business community that pays the merchandise processing fee. Moreover, Governor Ridge has stated that he anticipates "the rapid development of the ACE system will continue as will the interagency community's development of an International Trade Data System that creates a harmonized system for import-related data. These systems will likely become a cornerstone of the Department of Homeland Security's enterprise architecture."

Sec. 418: The recommendation requires that the Administration provide a separate budget request on the customs revenue functions within the new Department.

This recommendation is consistent with the overall approach of the Committee in assuring that the core revenue-collecting components of the Customs Service are maintained. Coupled with the cost accounting system that will record expenditures for customs revenue services, this requirement for a separate budget request will ensure that the Committee can continue to oversee that revenue is properly collected and trade is continuing appropriately.

Sec. 419: The recommendation would change the merchandise entry process to authorize monthly billing with a prohibition against deferral of duty past a statutory deadline.

This provision is a general reform of the import process. The purpose is to modernize the customs system from an antiquated entry-by-entry billing method to a modern monthly billing method that is more consistent with general business practice. Congress provided regulatory flexibility to the Executive Branch in the Customs Modernization Act to implement a modern billing system; however, there has been insufficient progress to date. In addition, the Administration has twice this year used the underlying statute (19 U.S.C. 1505(a)) in what the Committee believes is an inappropriate ad hoc manner to defer duties for extraordinary lengths of time. The provision creates a statutory deadline that may not be extended.

This provision is appropriate for the Homeland Security bill because it supports the overall goal of a modern, automated import system that will be used for commercial and homeland security purposes. Moreover, there is a further benefit in that the process of collecting import data and determining admissibility (linked closely to a homeland security mission) becomes more clearly removed from the collection of revenue (the traditional customs revenue mission).

Sec. 420: The recommendation defines customs revenue functions to include the assessing and collecting of all types of duties, fees, and taxes; the processing and denial of entry of persons and goods; enforcing quota, marking, and intellectual property laws; collecting trade data; enforcing trade agreements; functions of certain revenue collecting specialists; and functions of certain revenue collecting support offices.

These definitions are used throughout the recommended amendment in order to 1) define the scope of the newly created Customs Service core within the Department of Homeland Security and its directions for the Department's future operations related to trade and revenue collection; 2) describe to the scope of the authorities retained by the Department of the Treasury for delegation to the Secretary of Homeland Security; and 3) describe the services that must be maintained by the Department of Homeland Security even outside the newly-created Customs Service core.

Sec. 421: The recommendation provides that GAO will report on all trade functions performed by the executive branch.

The creation of a new Department that will have significant trade responsibilities has led the Committee to recommend a comprehensive report to identify all agencies in the executive branch that have trade functions. This report will assist the Committee in continuing to conduct oversight of international trade functions.

Sec. 422: The recommendation provides that Customs is prohibited from entering into new contracts with publicly traded corporations if the corporation is incorporated in a tax haven country as defined in the section, subject to the President's power to waive based upon national security reasons.

Dissenting Views
On the Chairman's Proposed Amendment to H.R. 5005
July 11, 2002

While the Administration's current focus is on the creation of the new Department of Homeland Security (DHS), the Ways & Means Committee is responsible for the Customs Service functions under the new Department. This includes the need to ensure that Customs employees' labor protections are maintained. And as Members of Congress, we are responsible for ensuring that the creation of this new department does not trample on existing laws and our democratic process. The absence of civil service and Freedom of Information Act protections in the Chairman's mark is ample reason to reject the amendment. But the hasty fashion in which this new agency is being developed is completely unacceptable under a democratic rule of law.

We commend the Chairman for attempting to preserve the revenue-raising functions of the Customs Service as a distinct entity within Customs. However, the Chairman's amendment only includes a small subsection of existing Customs personnel and includes a limited mandate. Although the Administration continues to reiterate its promise that Customs employees' civil service, collective bargaining, and whistle-blower protections will be maintained under the reorganized agency, these protections were not specifically included in the Chairman's amendment. While the Chairman advised the Committee that these protections do not fall under the Ways & Means jurisdiction, our support cannot rest on a mere promise from the Administration. Twenty-two existing federal agencies are targets for inclusion under the new DHS umbrella. We would discourage our colleagues from taking a cavalier approach with the lives of tens of thousands of civil servants for the sake of meeting a September 11 deadline.

Nothing in the Chairman's mark ensures that the Freedom of Information Act, the Federal Advisory Committee Act and the Government in Sunshine Act are maintained in the new Customs department under the DHS. As envisioned by the Administration, this leaves the option of closed-door meetings and secrecy up to the discretion of sixteen assistant secretaries for the new agencies—ten of whom would not need Senate confirmation to hold their posts.

There is no reason that the new department needs to be hastily rushed through the Ways & Means Committee, nor any other Congressional committee. This Committee held a hearing two weeks ago in which the Department of Treasury representative provided very little detailed information on the structure and components of the new Customs agency under DHS. Two weeks later, the same representative could not provide any additional information on the new Customs agency. The checks and balances established by our country's founding fathers should not be ignored in pursuit of meeting a self-imposed September 11 deadline.

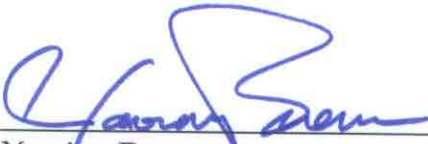
We wish to make perfectly clear that our dissension must not be interpreted as opposition to securing our domestic territories under the new Department of Homeland Security, but rather as an exercise in maintaining the checks and balances so crucial to the democratic process. This is the largest overhaul of the executive branch in fifty years and will have ramifications long beyond our tenure as Members of Congress. Any new department should be fashioned correctly the first time with all the sunlight the democratic process can afford. Regretfully, perfecting amendments offered during the Committee markup were rejected along party lines. In conclusion, the Chairman's amendment to H.R. 5005 does not provide the necessary elements for a long-standing democratic Department.



Pete Stark
Member of Congress



Jim McDermott
Member of Congress



Xavier Becerra
Member of Congress